

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

WISCONSIN ENERGY CORPORATION,)
INTEGRYS ENERGY GROUP, INC.,)
PEOPLES ENERGY, LLC, THE PEOPLES)
GAS LIGHT AND COKE COMPANY,)
NORTH SHORE GAS COMPANY, ATC)
MANAGEMENT INC., and AMERICAN)
TRANSMISSION COMPANY LLC)

Application pursuant to Section 7-204 of the)
Public Utilities Act for authority to engage in a)
Reorganization, to enter into agreements with)
affiliated interests pursuant to Section 7-101, and)
for such other approvals as may be required under)
the Public Utilities Act to effectuate the)
Reorganization.)

Docket No. 14-_____

Direct Testimony of

SCOTT J. LAUBER

Vice President and Treasurer –
Wisconsin Energy Corporation

On Behalf of
Wisconsin Energy Corporation

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1 **I. INTRODUCTION AND BACKGROUND**

2 **A. Witness Identification**

3 **Q. Please state your name and business address.**

4 A. My name is Scott J. Lauber. My business address is Wisconsin Energy Corporation, 231
5 West Michigan Street, Milwaukee, Wisconsin 53203.

6 **Q. By whom and in what capacity are you employed?**

7 A. I am the Vice President and Treasurer of Wisconsin Energy Corporation (“Wisconsin
8 Energy”).

9 **Q. What are your duties in your position as the Vice President and Treasurer of**
10 **Wisconsin Energy?**

11 A. I am responsible for long-range financial planning, forecasting and managing the utilities’
12 revenue requirements, as well as oversight of Wisconsin Energy’s treasury and cash
13 management functions. I have also been involved in preparing many of the financial
14 aspects of a rate case, including evaluation of budgets, sales forecasting, and
15 determination of revenue deficiencies.

16 **B. Purpose of Testimony**

17 **Q. What is the purpose of your testimony in this proceeding?**

18 A. The purpose of my testimony is to discuss: (1) accounting issues associated with
19 Wisconsin Energy’s acquisition of Integrys Energy Group, Inc. (“Integrys”) to create a
20 new holding company, WEC Energy Group, Inc. (“WEC Energy Group”) (referred to
21 herein as the “Transaction”) and its impact on The Peoples Gas Light and Coke Company
22 (“Peoples Gas”) and North Shore Gas Company (“North Shore”) (the “Reorganization”);

(2) Wisconsin Energy's strong credit rating and how the Reorganization will not impair Peoples Gas' and North Shore's (collectively, the "Gas Companies") credit ratings or ability to raise capital on reasonable terms; (3) whether other provisions of the Illinois Public Utilities Act (the "Act") are applicable to financing issues related to the Reorganization; (4) the timing and impact on the Gas Companies' customers of synergies resulting from the Reorganization and the costs to achieve those synergies, as well as their allocation; and (5) the post-Reorganization structure of affiliate agreements affecting the Gas Companies and how costs will be properly allocated to ensure that there is no subsidization of one affiliate by another.

C. Summary of Conclusions

Q. Please summarize the conclusions of your direct testimony.

A. I conclude:

(1) The Illinois Commerce Commission (the "Commission") should approve the accounting entries that will potentially be recorded on the Gas Companies' books as a result of the Transaction, if necessary.

(2) The Reorganization will not significantly impair the ability of the Gas Companies to raise necessary capital on reasonable terms or to maintain a reasonable capital structure, nor will the Reorganization significantly impact the credit quality, cost of financing, or access to the capital markets of the Gas Companies.

(3) There are no other provisions of the Act that the Commission must consider with respect to financing issues related to the Reorganization.

(4) Wisconsin Energy does not seek the recovery of any of the costs incurred to accomplish the Reorganization. Further, there will not be any immediate savings for the Gas Companies resulting from the Reorganization, and any savings that may be achieved

47 as a result of the Reorganization will not occur for several years. The Commission
48 should approve the Joint Applicants' proposal concerning the allocation of the savings,
49 whereby the net savings achieved by the Gas Companies if any, as a result of the
50 Reorganization will flow to customers by being reflected in the determination of the Gas
51 Companies' test year costs of service in their subsequent rate cases.

52 (5) The Commission should approve WEC Energy Group's and the Wisconsin
53 Energy companies' execution of an agreement substantially similar to the Commission-
54 approved Integrys Affiliated Interest Agreement. This agreement, together with other
55 affiliated interest agreements to be entered into that do not need Commission approval
56 because they do not involve the Gas Companies and the existing Integrys affiliated
57 interest agreements, will ensure that costs are fairly allocated between utility and non-
58 utility activities, and that the Reorganization will not result in the subsidization of non-
59 utility activities by the Gas Companies or their customers.

60 **D. Itemized Attachments to Direct Testimony**

61 **Q. Are you sponsoring any exhibits with your direct testimony?**

62 **A.** Yes. I have attached the following exhibits to my testimony:

- 63 • A table showing the costs and fees attributable to the Reorganization as required
64 by Section 7-204A(a)(3) of the Act, attached as Joint Applicants Exhibit ("Ex.")
65 2.1;
- 66 • Interim WBS Regulated Affiliated Interest Agreement, attached as Joint
67 Applicants Exhibit Ex. 2.2
- 68 • Interim WBS Non-Regulated Affiliated Interest Agreement, attached as Joint
69 Applicants Ex. 2.3; and

- WEC Energy Group Affiliated Interest Agreement, attached as Joint Applicants Ex. 2.4.

E. Background and Experience

Q. Please describe your educational and business experience.

A. I have a Bachelors of Business Administration in Accounting from the University of Wisconsin-Whitewater. I am also a Certified Public Accountant.

Prior to joining Wisconsin Energy, I worked as a staff auditor at Arthur Anderson. I have held several roles in the 24 years since I joined Wisconsin Energy, most in the Finance and Accounting Department. I was in charge of Corporate Accounting and Budgeting which included external reporting; I was the Delivery Business Unit Controller; and most recently I held the Assistant Treasurer position.

II. ACCOUNTING ISSUES

Q. Will there be accounting entries on the books and records of Peoples Gas and North Shore as a result of the Reorganization?

A. At the present time, the Joint Applicants do not anticipate any entries needing to be recorded. Our analysis, however, is not yet complete and is subject to review by both our independent auditors and the Securities and Exchange Commission (“SEC”). The purchase accounting rules of the SEC generally require what is known as “push-down accounting” for business combinations, such that the separate financial statements of a subsidiary would reflect any fair value adjustments required to be made along with good will attributable to the subsidiary. The SEC rules, however, allow an exception to push-down accounting if certain conditions are met. If those conditions are met, a subsidiary, such as Peoples Gas and North Shore, can elect not to reflect push-down accounting in

93 their separate financial statements. The primary condition that permits the exception to
94 push-down accounting for business combination requirements is if the subsidiary has
95 significant public debt outstanding, which we currently believe to be the case with
96 Peoples Gas and North Shore. As such, assuming all of the conditions are met, we intend
97 to apply the exception and not reflect the impact of the acquisition on the books and
98 financial statements of the Gas Companies.

99 It is anticipated that there will be three primary impacts to the books and records
100 of the Gas Companies that will be recorded if push-down accounting is required to be
101 recorded in accordance with accounting principles generally accepted in the United States
102 of America (“GAAP”). These impacts are as follows:

- 103 • Debt on the Gas Companies’ balance sheets must be recorded at its fair
104 value, with fair value determined at the time of closing of the Transaction.
105 The difference between carrying value and fair value will be amortized on
106 the effective interest method over the remaining term of the debt. The
107 difference between the book cost of the debt and the market value of the
108 debt would be recoded as a regulatory asset or liability and amortized over
109 the life of the debt to ensure this transaction does not affect the cost of
110 debt for ratemaking purposes.
- 111 • The net asset or liability associated with the post-retirement and post-
112 employment benefit plans will be reflected at fair value at the time of
113 closing. The difference between carrying value and fair value will be
114 recorded as a regulatory asset or liability and amortized over future
115 periods consistent with the Gas Companies’ past practices.

- The difference between the acquisition price and fair values assigned to assets and liabilities will be recorded as goodwill. Because the Gas Companies are regulated entities, the historical basis of assets and liabilities, except for those noted above, is considered to be fair value under GAAP.

Q. If push-down accounting is required, how will the goodwill recorded on the Gas Companies' financial statements be financed?

A. If push-down accounting is required, the goodwill associated with the Reorganization will be recorded as an equity contribution from the parent corporation. Therefore, if that occurs, the equity ratio of the Gas Companies will be higher than they are today for book purposes. For future rate-setting procedures, Wisconsin Energy anticipates that any goodwill assets and related equity balances will be disregarded in determining the overall cost of service for Peoples Gas and North Shore. This will ensure that the push-down has no effect on the common equity ratios of the Gas Companies for ratemaking purposes.

Q. Can you provide these accounting entries at this time?

A. No. While I have introduced the nature of the journal entries that could be required as part of the Reorganization, the details of the accounting entries will not be known until the Transaction closes. The final accounting entries will not be known until that time for two reasons. First, the ultimate purchase will be based upon the fair value of Wisconsin Energy common stock as of the closing date. Second, the fair value of the net assets acquired will also be measured as of the closing date. The actual numbers are dependent on the measurement date, which in this case will be the date of closing, as they are all dependent on fair value measurements. These entries will be disregarded for the

purposes of ratemaking, and none of the entries will have an impact on the credit ratings – and thus the cost of capital – of the Gas Companies.

Q. Is there any other accounting issue you would like to address at this time?

A. Yes. As discussed by Mr. Allen Leverett in his direct testimony (Joint Applicants Ex. 1.0), the Gas Companies will remain separate Illinois public utilities regulated by the Commission, and remain subject to all applicable laws, regulations, rules, decisions, and policies governing the regulation of public utilities in Illinois. Accordingly, this means that the Gas Companies will continue to adhere to the Commission's Uniform System of Accounts for Gas Utilities.

III. FINANCING CAPABILITIES AND ACCESS TO CAPITAL MARKETS

Q. Please describe the financial condition of Wisconsin Energy.

A. Before taking into account the Transaction, Wisconsin Energy is a Fortune 1000 corporation with an equity market capitalization of \$10.5 billion, and total assets of \$14.8 billion, as of March 31, 2014. Wisconsin Energy is a New York Stock Exchange-listed company that is solidly positioned to maintain its existing strong investment-grade credit ratings and its longstanding track record of earnings and dividend growth. Wisconsin Energy and its affiliates have access to capital markets and have been able to generate funds internally and externally to meet their capital requirements. Wisconsin Energy and its subsidiaries maintain bank back-up credit facilities to provide liquidity support for each company's obligations with respect to commercial paper and for general corporate purposes. As of March 31, 2014, Wisconsin Energy had approximately \$1.2 billion of available, undrawn lines under its bank back-up credit facilities, and approximately \$422.2 million of commercial paper outstanding, on a consolidated basis that was

supported by the available lines of credit. Wisconsin Energy's senior unsecured debt is rated A2/BBB+/A- by Moody's, Standard & Poor's and Fitch, respectively. Wisconsin Energy's commercial paper program is rated P1/A2/F2 by Moody's, Standard & Poor's and Fitch, respectively.

Q. Will the Reorganization impair the ability of the Gas Companies to raise necessary capital on reasonable terms or to maintain a reasonable capital structure?

A. No, it will not. Peoples Gas and North Shore will continue to maintain their current long-term debt profiles. As discussed in the testimony of witness Mr. John Reed (Joint Applicants Ex. 3.0) and below in my testimony, the Reorganization will have no impact on the credit ratings of the Gas Companies.

Q. How will the Gas Companies' access to equity markets be affected by the Reorganization?

A. As exists today, the Gas Companies will have access to the equity markets through their parent company. Today that parent company is Integrys Energy Group, Inc. ("Integrys"). Following the consummation of the Reorganization, that access will come through the parent new holding company to be created by the Transaction – WEC Energy Group, Inc. ("WEC Energy Group"). WEC Energy Group will be a significantly larger entity (one that likely will be a Fortune 500 company and is expected to continue to be included in the S&P 500 index), with continued strong financial profile, that should have improved stock liquidity, which will make the stock more attractive to larger institutional investors who typically require the ability to buy and sell stocks in large-volume blocks. At a minimum, the improved liquidity, combined with a strong financial profile, is expected to

maintain the combined company's ability to raise equity as compared to Wisconsin Energy's current ability and may actually improve it.

Q. What do you expect will be the impact of the Reorganization on the credit quality for WEC Energy Group and the Gas Companies?

A. I do not expect that the Reorganization will result in a significant, if any, degradation of the credit quality of the new holding company, WEC Energy Group. After the Reorganization was announced, the credit ratings for Wisconsin Energy were affirmed, although with a credit watch and "negative outlook," indicating that there could be a slight downward revision given the size of the acquisition being undertaken. Even if some slight downgrade occurs after the Reorganization is closed, WEC Energy Group will continue to have ready access to the capital markets. Significantly, the credit rating agencies affirmed the current credit ratings of Wisconsin Energy's and Integrys' utilities, including the Gas Companies.

Q. Because the daily business funding requirements, including seasonal working capital needs, for the Gas Companies are dependent upon access to the commercial paper markets, what impact will the Reorganization have on the Gas Companies' commercial paper ratings?

A. The Reorganization should have no impact on the Gas Companies' commercial paper ratings. As stated, the credit rating agencies have affirmed the Gas Companies' credit ratings. These ratings will allow the Gas Companies to continue accessing the daily commercial paper market as needed.

205 **Q. How does Wisconsin Energy propose to manage the short-term working capital**
206 **needs of the Gas Companies following the consummation of the Reorganization?**

207 A. Wisconsin Energy proposes to maintain the Gas Companies' current lines of credit and
208 commercial paper programs to fund the short-term and seasonal working capital
209 requirements of the Gas Companies in the fashion substantially similar to the Gas
210 Companies' current programs. Following the consummation of the Reorganization, we
211 will review the needs of the Gas Companies to determine the appropriate short-term
212 instruments necessary to fund their general working capital requirements.

213 **Q. Will the capital requirements or capitalization of the Gas Companies change with**
214 **the Reorganization?**

215 A. Currently we do not believe so. We believe that the capital requirements of the Gas
216 Companies forecasted for the five years following the close of the Reorganization, as
217 shown in Joint Applicants Exs. 4.1 and 4.2, will remain unchanged. Further, based on
218 our current analysis, we believe we will meet the requirements to apply the exception
219 afforded by the SEC related to the "push-down" of goodwill and other adjustments to the
220 books of the Gas Companies related to this transaction, as I discussed earlier in my
221 testimony.

222 **IV. OTHER FINANCING PROVISIONS UNDER THE ACT**

223 **Q. Have you reviewed, or had reviewed under your direction, the Act for any other**
224 **potential requirements applicable to financing issues related to the Reorganization?**

225 A. Yes. In general, provisions involving financing relate to rate case issues or Commission
226 approval for the issuance of debt or equity. For example, the requirements of Section 9-
227 230 of the Act appear to prescribe the factors the Commission should consider, or more

specifically, not consider, in determining the rate of return for public utilities in the context of a rate proceeding. I do not believe Section 9-230 requires consideration in this case as the Commission is not setting a rate of return for the Gas Companies in this particular proceeding. After review, we have concluded that there are not other requirements in the Act applicable to the financing issues related to the Reorganization that the Commission needs to consider as part of this proceeding.

V. REORGANIZATION COSTS AND SAVINGS

Q. Have the Joint Applicants identified the “costs and fees attributable to the reorganization” as required by Section 7-204A(a)(3) of the Act?

A. Yes. The costs and fees attributable to the reorganization are shown in Joint Applicants Ex. 2.1. As stated in the direct testimony of Joint Applicants’ witness Mr. Leverett (Joint Applicants Ex. 1.0), Wisconsin Energy commits that it will not seek the recovery of the costs incurred to accomplish the Reorganization – *i.e.*, Transaction, Change in Control, Financing and Legal/Other Professional costs – from customers. Nor will Wisconsin Energy seek recovery of the acquisition premium paid as part of the Transaction in rate base, nor the amortization of the premium in future cost of service determinations.

Q. How will Reorganization costs be reflected on the books and records of the Gas Companies?

A. The costs of the Reorganization will be recorded as incurred and allocated in accordance with existing and proposed affiliated interest agreements and services agreement discussed in the following section of my testimony.

250 **Q. How will the Reorganization costs recorded on the books and records of the Gas**
251 **Companies be considered for ratemaking purposes?**

252 A. As discussed in the direct testimony of Joint Applicants' witnesses Mr. Leverett (Joint
253 Applicants Ex. 1.0) and Mr. Reed (Joint Applicants Ex. 3.0), Wisconsin Energy does not
254 anticipate and cannot identify any immediate material savings to result after the close of
255 the Reorganization. As discussed by those witnesses, the Reorganization is not one based
256 upon synergies, such as occur when a corporate acquisition results in large layoffs of
257 employees. This is demonstrated here by Wisconsin Energy's commitment to
258 maintaining a level of Full Time Equivalents in Illinois for a set period of time following
259 the close of the Reorganization. Those savings will not occur immediately upon the
260 closing of the Reorganization in 2015, and likely will not occur for several years
261 thereafter. Indeed, based on Mr. Reed's analysis, net savings in the holding company
262 system's non-fuel/non-commodity O&M costs likely will not result from the
263 Reorganization until after a "ramp up" period of 5-10 years after the Reorganization
264 closes. Nevertheless, it is anticipated that at some point years after the close of the
265 Reorganization, there will be net savings achieved as a result of the Reorganization. Mr.
266 Reed explains how such savings are likely to occur in his testimony. When such savings
267 are achieved, they will result in the Gas Companies' costs of service being lower than
268 they otherwise would be if the Reorganization had not taken place. It is Wisconsin
269 Energy's proposal that such savings be flowed back to customers as part of the
270 ratemaking process whenever the Gas Companies file requests to change their base rates
271 subsequent to the close of the Reorganization. In this way, net savings achieved by the
272 Gas Companies if any, as a result of the Reorganization will be allocated to customers by

being reflected in the determination of the Gas Companies' test year costs of service when their base rates are set subsequent to the Reorganization. Because there will be no net savings during the period in which Wisconsin Energy is committing not to seek a change in the Gas Companies' base rates, this approach will capture and allocate to customers any savings resulting from the Reorganization.

VI. AFFILIATED INTEREST AND SERVICE AGREEMENTS

Q. Please describe the current state of arrangements between Wisconsin Energy's subsidiaries, and between Integrys' subsidiaries.

A. Currently, Wisconsin Energy and its subsidiaries share services pursuant to a series of affiliated interest agreements, including a Master Service Agreement between Wisconsin Energy and each of its subsidiaries and a Master Service Agreement between Wisconsin Energy's utility subsidiaries, along with several other affiliated interest agreements existing between Wisconsin Energy affiliates pertaining to specific operations in Wisconsin. The Integrys system includes a centralized services company, Integrys Business Support, LLC ("IBS"), that provides a defined suite of shared services to the holding company and all of the operating companies. The non-IBS Integrys companies may also provide services to each other and to IBS under a separate affiliated interest agreement.

Q. What are the Joint Applicants' plans with respect to transitioning and integrating these two systems after the Reorganization closes?

A. The Reorganization will not affect the existing relationship between IBS and today's Integrys companies, including the Gas Companies. At or shortly after closing IBS will become a direct subsidiary of WEC Energy Group and be renamed as WEC Business

Services, LLC (“WBS”). WBS will maintain the existing IBS affiliated interest agreements with today’s Integrys companies. Over time Wisconsin Energy expects that WBS will provide WEC Energy Group and today’s Wisconsin Energy subsidiaries with an increasing range of services. However, adequate planning and implementation time will be required in order to begin the provision of each of the services that WBS will ultimately deliver to the Wisconsin Energy companies. Immediately after closing, the Joint Applicants expect that WBS will provide the Wisconsin Energy companies with senior management services and perhaps legal, accounting, human resources, finance, or other services.

Q. What agreements or modification of existing agreements are being proposed as part of the Reorganization to effectuate this plan?

A. The Joint Applicants propose that at or shortly after closing, WEC Energy Group and today’s Wisconsin Energy subsidiaries will execute interim affiliated interest agreements that allow but do not require the Wisconsin Energy companies to take services from WBS. These interim agreements will be based on the existing Master IBS Regulated and Non-Regulated Affiliated Interest Agreements. The only substantive changes are to ensure that the Wisconsin Energy companies are not overcharged under the general/corporate cost allocators under the interim agreements. Copies of these agreements, the Interim WBS Regulated Affiliated Interest Agreement and Interim WBS Non-Regulated Affiliated Interest Agreement, accompany my testimony as Joint Applicants Exs. 2.2 and 2.3, respectively. These agreements will allow the Wisconsin Energy companies to begin receiving services from WBS immediately under terms and conditions already approved by this Commission. Because the Gas Companies will not

319 be parties to these proposed agreements, it is our understanding that Commission
320 approval is not required for these agreements.

321 In addition, WEC Energy Group and today's Wisconsin Energy subsidiaries will
322 execute an agreement substantially similar to the Commission-approved Integrys
323 Affiliated Interest Agreement. A copy of the proposed WEC Energy Group Affiliated
324 Interest Agreement is attached to my testimony as Joint Applicant Ex. 2.4. The WEC
325 Energy Group Affiliated Interest Agreement will allow services to be provided by
326 Wisconsin Energy companies to Integrys companies, including the Gas Companies, and
327 by Integrys companies, including the Gas Companies, to Wisconsin Energy companies,
328 all pursuant to appropriate contractual requirements, allocation standards and compliance
329 processes. The Joint Applicants request approval of this agreement. The WEC Energy
330 Group Affiliated Interest Agreement will replace the existing WEC Master Service
331 Agreements, which will be terminated so that the Wisconsin Energy companies provide
332 each other services under this single affiliated interest agreement.

333 **Q. Do the proposed agreements allow the Commission to make the findings required**
334 **under Section 7-204(b)(2) and Section 7-204(b)(3) of the Act?**

335 A. Yes. Section 7-204(b)(2) of the Act requires the Commission to find "the proposed
336 reorganization will not result in the unjustified subsidization of non-utility activities by
337 the utility or its customers. 220 ILCS 5/7-204(b)(2). Section 7-204(b)(3) of the Act
338 requires the Commission to find "costs and facilities are fairly and reasonably allocated
339 between utility and non-utility activities in such a manner that the Commission may
340 identify those costs and facilities which are properly included by the utility for
341 ratemaking purposes. 220 ILCS 5/7-204(b)(3) As described above, the Reorganization

will not materially change the contractual arrangements in place with respect to the Gas Companies that, where appropriate, have been reviewed and approved by the Commission to ensure there will not be unjustified subsidization of non-utility activities by the utility or its customers, as well that the allocation of costs and facilities is done in a manner that allows the Commission to properly identify them for ratemaking purposes. The Commission should approve the WEC Energy Group Affiliated Interest Agreement so that the relationships among and between the Gas Companies, WEC Energy Group, and its other subsidiaries will be governed by the same contractual terms that already have been approved by the Commission. Further, the cost allocation methodologies in the existing Master Regulated and Non-Regulated Affiliated Interest Agreements, and proposed Interim WBS Regulated and Non-Regulated Affiliated Interest Agreements, will ensure that there is no subsidization of costs and that the costs are fairly allocated and easily identifiable. The processes and procedures that will be in place will ensure transparency of charges and appropriateness of charges remaining in the Gas Companies.

VII. CONCLUSION

Q. Does this conclude your testimony?

A. Yes, it does.